Supreme Court, U.S.
FILED
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No. 95-846

Supreme Court of the United States

OCTOBER TERM, 1995

ALVIS M. RUSHTON,

Petitioner,

V.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

ALVIS M. RUSHTON
806 Shady Ridge Drive
Cedar Hill, TEXAS 75104
(214) 291-6677

Petitioner, In Propria Persona

QUESTION PRESENTED

Does the clear, precise and squarely in point language of Title 26 U.S.C. §6244 adopt, engraft and incorporate 26 U.S.C. §6231(a)(1)(B)(i)(I), the small partnership exemption, into the "S" corporation audit and administrative procedures §§6241-6245 of the Internal Revenue Code, or in other words, should this Court decline "the importunity of the Commissioner of Internal Revenue that we interpret a statute clear on its face to convey a different meaning"[1]?

PARTIES TO THE PROCEEDING

The parties to the proceeding are those in the caption (Petitioner-Appellant, Alvis M. Rushton and Respondent-Appellee, Commissioner of Internal Revenue.

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[1] *Arenjay Corp. v. Commissioner of Internal Revenue*, 920 F.2d 269 (5th Cir. 1991) at 270

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No. .....

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1995

ALVIS M. RUSHTON,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE

Respondent.

PETITION FOR WRIT OF CERTIORARI

TO THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

Petitioner herein respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered in this action on July 7th, 1995.

OPINIONS BELOW

The decision of the Tax Court is reported at T.C. Memo. 1993-179. The decision of the court of appeals is unpublished under Ninth Circuit Docket No. 94-70280 (Appendix Pages A-1 to A-3).

BASIS FOR JURISDICTION

The final judgment of the court of appeals was entered on July 7, 1995. Petition for rehearing was denied in an Order entered September 27, 1995 (Appendix Page A-4 to A-5). This Court has jurisdiction to review the judgment of the court of appeals pursuant to 28 U.S.C. §1254(1).

APPLICABLE STATUTES

Title 26 U.S.C. (Internal Revenue Code)

Subchapter D -
Tax Treatment of Subchapter S Items

. . .

"I.R.C. §6244. Certain partnership provisions made applicable.

"The provisions of --

(1) subchapter C which relate to

(A) assessing deficiencies, and filing claims for credit or refund, with respect to partnership items, and

(B) judicial determination of partnership items, and

(2) so much of the other provisions of this subtitle as relate to partnership items, are (except to the extent modified or made inapplicable in regulations) hereby extended to and made applicable to subchapter S items."

. . .

Subchapter C -
Tax Treatment of Partnership Items

. . .

"I.R.C. §6231. Definitions and special rules.

(a) Definitions.

For the purposes of this subchapter -

(1) Partnership

(A) In general. Except as provided in subparagraph (B), the term 'partnership' means any partnership required to file a return under section 6031(a).

(B) Exception for small partnerships.

(i) In general. The term 'partnership' shall not include any partnership if --

(I) such partnership has 10 or fewer partners each of whom is a natural person (other than a nonresident alien) or an estate, and

(II) each partner's share of each partnership item is the same as every other item.

For the purposes of the preceding sentence, a husband and wife (and their estate) shall be treated as 1 partner.

(ii) Election to have subchapter apply. A partnership (within the meaning of subparagraph (A) may for any taxable year elect to have clause (i) not apply. Such election shall apply for such taxable year and all subsequent taxable years unless revoked with the consent of the Secretary.

(2) Partner. The term "partner" means -

(A) a partner in a partnership, and

(B) any other person whose income tax liability under subtitle A is determined in whole or in part by taking into account directly of indirectly partnership items of the partnership.

(3) Partnership item. The term 'partnership item' means, with respect to a partnership any item required to be taken into account for the partnership's taxable year under any provisions of subtitle A to the extent regulations prescribed by the Secretary provide that for the purposes of this subtitle, such item is more appropriately determined at the partnership level than at the partner level.

(4) Nonpartnership item. The term 'nonpartnership item' means an item which

is (or is treated as) not a partnership item.

. . .

(c) Regulations with respect to certain special enforcement areas.

. . .

(2) Items may be treated as nonpartnership items.

To the extent that the Secretary determines and provides by regulations that to treat items as partnership items will interfere with the effective and efficient enforcement of this title in any case described in paragraph (1), such items shall be treated as nonpartnership items for purposes of this subchapter."

. . .

STATEMENT OF THE CASE

The corporation in which Petitioner-Appellant Rushton has 100% ownership interest is the "S" corporation under 26 U.S.C. §1361 (Internal Revenue Code), Twenty-Three Nineteen Creekside, Inc. The "S" corporation's records were examined by Respondent-Appellee, Commissioner of Internal Revenue under unified partnership administrative procedures, I.R.C. §6241-6245.

For the sole purpose of expediting appeal and avoiding costs of trial litigation, all issues were stipulated with the exception of jurisdiction under §§6231(a)(1)(B)(i)(I), 6244 "small partnership exemption" from unified procedures, *N.B. Arenjay Corp.* 920 F.2d 269 (5th Cir. 1991) establishing the small "S" corporation exemption from unified partnership procedures.

As applicable to Petitioner's individual income tax return, the Statute of Limitations under I.R.C. §6501(a) has expired.

The Tax Court ruled, "As we have previously stated, 'There are no exceptions written into the statutory language for subchapter S corporations based upon the number of shareholders,'" citing *Eastern States Casualty Agency, Inc.* 96 T.C. 773 at 782 (*Twenty-Three Nineteen Creekside, Inc.*, T.C. Memo. 1993-179).

Petitioner-Appellant Rushton appealed the above Tax Court decision to the United States Court of Appeals for the Fourth Circuit based on the Final "S" Corporation Administrative Adjustment dated 21 DEC 1989 being mis-addressed c/o:

ALVIS M. RUSHTON
Tax Matters Person
103 CRESSTON ROAD
ARNOLD, CA 21012

instead of 103 CRESSTON ROAD, ARNOLD, MD 21012 as shown on the Tax Court Petition filed March 15, 1990, under 26 U.S.C. §7482(b)(1)(E).

The Fourth Circuit transferred venue to the Ninth Circuit, which rejected the Fifth Circuit's position in *Arenjay, supra;* endorsed the opinion of the Tax Court majority in *Eastern States Casualty, supra;* and adopted, essentially without discussion, the Eleventh Circuit's decision in *Beard* 992 F.2d 1516 and in the Tenth Circuit's *Home of Faith* 39 F.3d 263.

REASONS FOR GRANTING THE WRIT

I. DIRECTLY IN CONFLICT WITH THE DECISION OF THE NINTH CIRCUIT IN THE INSTANT CASE ON THE SAME MATTER IS THE DECISION OF THE COURT OF APPEALS FOR THE FIFTH CIRCUIT IN *ARENJAY CORP. V. C.I.R.*, 920 F.2d 269.

There is a manifest conflict of opinion between United States Courts of Appeal for different circuits on the same matter. As far as maintaining a clear, precise and reliable set of laws on small business taxation, the essential question is whether the clear, unambiguous language of the statute in §6244 was effective forthwith, or whether belated, contradictory regulations under §6241 should be granted greater importance, overriding a "statute clear on its face," *Arenjay, supra*, at 270.

The position of Petitioner-Appellant Rushton (and of the Fifth Circuit) is plain, clear, and straightforward: §6244 was clear and unambiguous in engrafting §6231(a)(1)(B)(i)(I), the small partnership

exemption, without any need of "interpretive regulation" to enhance the clear language of the statute.

In the words of *Arenjay, supra*, Petitioner-Appellant Rushton prays this Court decline "the importunity of the Commissioner of Internal Revenue that we interpret a statute clear on its face to convey a different meaning":

> "Declining the importunity of the Commissioner of Internal Revenue that we interpret a statute clear on its face to convey a different meaning because in the Commissioner's opinion, unsupported by the record evidence, the patent reading would lead to absurd consequences, we hold that the procedural provisions of subchapter C of the Internal Revenue Code relating to partnerships apply to subchapter S corporations, and reverse the Tax Court judgment.
>
> . . .
>
> "Section 6231 (a) (1) (B) provides partnerships with ten or fewer partners with an exemption from audit and litigation procedures known as the 'small partnership exception.'
>
> . . .
>
> "Section 6231 of the statute is unambiguous. Partnerships with ten or fewer partners are exempted from the

> audit and litigation procedures. Congress grafted subchapter S onto the partnership provisions; §6231 is made applicable to S corporations by §6244. Thus S corporations are governed by the same rules applicable to partnerships. . . . Section 6231 exempts those partnerships with ten or fewer partners. By overlaying the word 'partnership' with 'S corporation,' and the word 'partner' with 'shareholder,' §6231 provides an '[e]xception for small S corporations . . . . if such corporation has ten or fewer shareholders. . . .'" *Arenjay, supra,* 270-271.

II. THE NINTH CIRCUIT HAS, IN ADOPTING THE *BEARD* OPINION ON I.R.C. §6241, ERRED IN APPLYING AN INADMISSIBLE STANDARD FOR ADJUDGING CLEAR AND UNAMBIGUOUS PROVISIONS OF I.R.C. §6244 (*ARENJAY*).

This Court has sustained, under the doctrine of express statutory subject matter scope, and held that the essence legislation is determined in the first instance in the plain language of the statute itself. When the statute is clear and unambiguous, the expressed intent of Congress is paramount: the statutory word unambiguously governs the court and regulatory agency alike. Board of

Governors v. Dimension Financial Corp., 474 U.S. 361, 368, 373 (1986)[2].

As affirmed by this Court, where the regulatory authority is acting outside the express subject matter scope of the statutory words of Congress, any extraneous action outside that scope is a nullity, an oxymoron, and requires a change by Congress in the statutory definition at hand. *Dimension Financial Corp. v. Board of Governors,* 744 F.2d 1402 (10th Cir. 1984) at 1409-1410.

The issuance of a regulation outside the express statutory subject matter scope of a Congressional statute cannot cure the exercise of powers denied by Congress or not provided for by Congress. Id., at 1410. *Arenjay, supra,* at 271; also *Dixon v. U.S.,* 381 U.S. 68, 74-75 (1965);

---

[2] Federal Reserve Board inclusion of "nonbank banks" in the category of "bank" in its Regulation Y is outside the express statutory subject matter scope of the unambiguous words of the Congressional statutory definitions.

Manhattan General Equipment Co. v. C.I.R., 297 U.S. 129, 134-135 (1936).

It is a fundamental principle of statutory construction that "the definition of a term in the definitional section of a statute controls the construction of that term whenever it appears throughout the statute." 1A Sutherland, *Statutory Construction* (5th ed.) (1992), §20.08, at 90, n. 10. See also *Board of Governors v. Dimension Financial Corp., supra,* at 374; *Florida Dept. of Banking & Finance v. Board of Governors,* 800 F.2d 1534, 1536 (11th Cir. 1986).

When Congress defines the language it uses, its definitions are binding, fixed and immutable upon the court. 1A Sutherland, *Statutory Construction, supra,* §20.08, at 90, n. 5. *Board of Governors v. Dimension Financial Corp., supra,* at 374; *Dimension Financial Corp. v. Board of Governors, supra,* at 1410; *Florida Dept. of*

Banking & Finance, supra, at 1536.

It is a fundamental principle of statutory construction, in addition, that "'effect must be given to every word, clause and sentence of a statute' so that no part will be inoperative or superfluous, void or insignificant." *In Re Surface Mining Regulation Litigation,* 627 F.2d 1346, 1362 (D.C. Cir. 1980), citing 2A Sutherland, *Statutory Construction* (4th ed.) (1973), §46.02.

Thus the §6231(a)(3) (Subchapter C) "partnership items" can pertain only and exclusively to those entities defined to be Subchapter C "partnerships" by §6231(a)(1)(B)(i)(I), which is the premise of this petition for writ of certiorari under this Court's doctrine of express statutory subject matter scope.

III. CONCLUSION

For the above reasons, a writ of certiorari should issue to review the Ninth Circuit decision entered July 7, 1995, or, in the alternative, this Court pursuant to Supreme Court Rule 16.1 should summarily reverse the Ninth Circuit's July 7, 1995 Memorandum and dismiss for want of jurisdiction the Tax Court decision, T.C. Memo. 1993-179.

Dated: November 27, 1995

Respectfully submitted,

/s/ ALVIS M. RUSHTON,

Alvis M. Rushton,

806 Shady Ridge Drive
Cedar Hill, TX 75104
(214) 291-6677

In Propria Persona

APPENDIX

FILED
JUL 7 1995
CATHY A. CATERSON, CLERK
U.S. COURT OF APPEALS

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

ALVIS M. RUSHTON,	)
	)
Petitioner-Appellant,	)
	)
v.	)
	)
COMMISSIONER OF INTERNAL REVENUE,	)
	)
Respondent-Appellee.	)

No. 94-70280

Tax Ct. No. 4787-90

MEMORANDUM*

Appeal from the United States Tax Court
William M. Fay, Tax Court Judge, presiding

Submitted February 15, 1995**
San Francisco, California

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* This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as provided by Ninth Circuit Rule 36-3.

** The panel unanimously finds this case suitable for decision without oral argument. Fed. R. App. P. 34 (a); 9th Cir. R. 34-4.

APPENDIX

Before: REINHARDT, THOMPSON and KLEINFELD, Circuit Judges.

Most of the issued raised in Mr. Rushton's appeal are controlled by our decision in the companion case, Twenty-Three Nineteen Creekside, Inc., v. Commissioner, -- F.3d -- (9th Cir. 1995).

Mr. Rushton argues that the statute of limitations should run from the date his personal return was filed, not the date on which the corporation's return was filed. Mr. Rushton's brief makes no argument for why his own stipulation to extend the statute of limitations would not prevent him from raising the issue. The authority he cites, Bufferd v. CIR., 113 S. Ct. 927 (1993), prevents limitations from beginning to run before the relevant tax return was filed. It has no application to the facts in the case at bar. The IRS could not determine 2319 Creekside's tax from

Rushton's personal return.

Mr. Rushton argues that the IRS did not properly mail notice to him. Because actual notice was received in time to allow Rushton to file a timely petition with the Tax Court, he suffered no prejudice from any defect in the postage on his notice letter that would require reversal. McKay v. Commissioner, 886 F.2d 1237, 1238 (9th Cir. 1989).

We have considered and we reject all of Mr. Rushton's other arguments.

AFFIRMED.

APPENDIX

FILED
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U.S. COURT OF APPEALS

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

ALVIS M. RUSHTON,	)
	)
Petitioner-Appellant,	)
	)
v.	)
	)
COMMISSIONER OF INTERNAL REVENUE,	)
	)
Respondent-Appellee.	)

No. 94-70280

Tax Ct. No. 4787-90

ORDER

Before: REINHARDT, THOMPSON and KLEINFELD, Circuit Judges.

The panel has voted to deny the petition for rehearing and to reject the suggestion for rehearing en banc.

APPENDIX

The full court has been advised of their suggestion for rehearing en banc and no active judge has requested a vote on whether to rehear the matter en banc. Fed. R. App. P. 35.

The petition for rehearing is denied and the suggestion for rehearing en banc is rejected.

APPENDIX

FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

TWENTY-THREE NINETEEN CREEKSIDE, INC.; MICHAEL E. BALDIGO,	)
Petitioners-Appellants,	)
v.	)
COMMISSIONER OF INTERNAL REVENUE,	)
Respondent-Appellee.	)

No. 93-70687

Tax Ct. No.

2345-90

OPINION

Appeal from the United States Tax Court
William M. Fay, Tax Court Judge, Presiding

Argued and Submitted
February 15, 1995 --
San Francisco, California

Filed July 7, 1995

Before: Stephen Reinhardt, David R. Thompson and Andrew J. Kleinfeld, Circuit Judges.

Opinion by Judge Kleinfeld

APPENDIX

SUMMARY

Tax/Litigation and Procedure

The court of appeals affirmed a tax court judgment, holding that a regulation providing for shareholder level treatment of a small S corporation was not applicable to the tax year in issue. The court also held that, unless otherwise designated, the "tax matters person" is deemed to be the S corporation shareholder with the largest profits interest.

Appellant 2319 Creekside, an S corporation had three shareholders at the end of the fiscal year ending June 30, 1994. [sic] Appellant Michael Baldigo was the largest shareholder with 72 percent of the shares. Baldigo later sold his shares to another shareholder. In 1989, the IRS adjusted the income of the corporation for tax year 1984 and sent notice to Baldigo as the "tax matters person." Under the Internal Revenue Code, the tax matters person is required to act on behalf of the corporation for tax purposes.

Baldigo filed petitions for readjustment on behalf of the corporation, but denied he was the tax matters person. The tax court held that Baldigo was the tax matters person, and that the corporation had properly been given tax treatment at the entity, rather than the shareholder, level.

APPENDIX

[1] Regarding tax matters persons, the regulations pertaining to partnerships also apply to S corporations. Under these provisions, Baldigo was the tax matters person because there was no designated tax matters person and he had the "largest profits interest." [2] It did not matter that Baldigo had sold his shares and could no longer collect fees from the corporation. He was the largest shareholder during the year ending 1984.

[3] The general rule is that the tax treatment of S corporations is determined at the corporate level. Under 26 U.S.C. §6244 certain partnership tax procedures as they relate to partnership items are applicable to subchapter S corporations. [4] There is an exception to the entity rule for small partnerships, allowing tax treatment at the individual level. There is also an exception for small S corporations; however, this exception only applies to tax years on or after January 30, 1987.

[5] Baldigo argued that the small partnership exception was applicable to small S corporations through §6244. The circuits are split on this issue. [6] Section 6244 does not incorporate all of partnership law. It applies only to provisions relating to assessment of, to filing claims with respect to, and to the judicial determination of partnership items. It does not apply to the small partnership exception to subchapter S corporations.

[7] There was no small S corporation exception to the entity level treatment for the tax year in this case.

COUNSEL

Gary V. Judd, Petaluma, California, for the petitioners-appellants.

Gary R. Allen (On the Briefs), Assistant Attorney general, Tax Division, Washington, D.C., for the respondent-appellee.

OPINION

KLEINFELD: Circuit Judge:

The main issue in this case is whether tax treatment of a subchapter S corporation with five or fewer shareholders proceeds at the entity level or the shareholder level. A regulation provides for shareholder level treatment, but does not apply to the period at issue in this case. An issue of who is the "tax matters person" also arises.

I. FACTS

Twenty-three Nineteen Creekside, Inc. is a subchapter S corporation. During its fiscal year at issue in this case, ending June 30, 1984, Michael L. [sic] Baldigo owner 72% of its shares, Alvis M. Rushton owned 25%, and another individual owned 3%. After the fiscal year 1984 ended, Mr. Rushton acquired all the shares from the other two shareholders.

Near the end of the statute of

limitations period, the IRS obtained from Mr. Rushton and Mr. Baldigo their signed consent to extend the time to assess tax attributable to the corporation. Then in 1989, the IRS sent a notice of final S corporation administrative adjustment, proposing to adjust the income of the corporation upward by $206,733. Identical copies of the notice of adjustment were mailed to Mr. Baldigo at various addresses the IRS had for him and to the "Tax Matters person" at the corporation's address.

The Internal Revenue Code provides for designation of one of the individuals associated with a partnership or subchapter S corporation as "tax matters partner" or "tax maters person." *See* 26 U.S.C. §6231(a0(7); 26 U.S.C. §6244; 26 C.F.R. §301.6231(a)(7)-1. The tax matters person has authority to take various actions on behalf of the entity in dealings with the Internal Revenue Service. 26 U.S.C. §6226. Mr. Baldigo took the position that he was not the "tax matters person" for the corporation.

Despite his claim that he was not the tax matters person for the corporation, Mr. Baldigo took steps to preserve the corporation's rights. Within the 90 day period prescribed by 26 U.S.C. §6226 for petitions made by the tax matters person, Mr. Baldigo filed a petition in the Tax Court for readjustment. He claimed the IRS had erred in the disallowances of deductions and other determinations underlying the $206,733 adjustment. On the signature line, he signed as "Michael E. Baldigo for" the corporation. In the caption, a rubber stamp below his name says

"A Person(s) Other Than the Tax Matters Person." Mr. Baldigo filed a second petition for readjustment after the 90-day period. This second petition was filed in accord with the time limits prescribed for a person other than the tax matters person to obtain review. *See* 26 U.S.C. §6226(b).

Only the procedural disputes, not the amount of the tax, have been put at issue in this appeal. The Tax Court consolidated the two petitions, and decided after a hearing that Mr. Baldigo was the tax matters person. The Tax Court then held that tax treatment of the corporation was properly done at the entity, rather than the shareholder level.

II. ANALYSIS

All of the issues are questions of law, which we review de novo. *Ann Jackson Family Foundation v. CIR*, 15 F.3d 917, 920 (9th Cir. 1994).

1. Tax Matters Person

Mr. Baldigo took the position that Mr. Rushton, not he, was the tax matters person. The corporation had not designated a tax matters person for its fiscal year ending June 30, 1984, the year at issue. Mr. Baldigo owned a majority of the shares of stock during that fiscal year, although he sold out to Mr. Rushton a few months after the fiscal year ended.

[1] The Tax Code makes the provisions for selecting a tax matters person found in the partnership section applicable to S

corporations unless the Secretary changes the rules by regulation. 26 U.S.C. §6244. No altering regulations were written, so the partnership provisions control. Because Mr. Baldigo owner the "largest profits interest," and no other tax matters person was designated, the Tax Court properly determined that by operation of law, he was the tax matters person for the taxable year at issue. 26 U.S.C. §6231(a)(7); 26 U.S.C. §6244; 26 C.F.R. §301.6231(a)(7)-1(m)(2).

[2] Mr. Baldigo argues that he did not wish to be the tax matters person, because by October of 1984, he had sold all of his interest in the Corporation to Mr. Rushton and could not be assured of being paid for the work involved. This does not matter. The corporation did not designate a tax matters person for its taxable year ending June 30, 1984, so all that mattered under the statute was that Mr. Baldigo owned "the largest profits interest," and held that ownership "at the close of the that taxable year." 26 C.F.R. §301.6231(a)(7)-1T(m)(2). The phrase "taxable year" in the regulation refers, by the word "that," to the taxable year of the entity, not of the individuals owning interests in the entity.

> The tax matters *partner for any partnership taxable year* to which this paragraph (m) applies is the general partner having the largest profits interest in the partnership at the close of *that taxable year* ....

26 C.F.R. §301.6231(a)(7)-1T(m)(2)(emphasis added). This clarifies and is consistent with the statutory reference to the "taxable year involved." 26 U.S.C.

§6231(a)(7)(B). The issue differs from the limitations question period answered in *Bufferd v. Commissioner*, 113 S. Ct. 927 (1993). We therefore conclude that the Tax Court correctly determined that Mr. Baldigo was the tax matters person for 2319 Creekside's 1984 fiscal year and that the petition for readjustment was properly filed by Mr. Baldigo.

2. Individual or entity level

Subchapter S corporations are treated similarly for tax purposes to partnerships, but they are not the same in all respects. Mr. Baldigo and 2319 Creekside argue that for the year at issue, they are entitled to tax administration at the individual rather than the entity level, like a partnership with ten or fewer partners. We affirm the Tax Court's determination that entity level administration was correct.

[3] The controlling statutes expressly grant the Secretary the power to resolve the matters at issue by regulations. The general rule, that subchapter S corporations' tax treatment is determined at the corporate level, expressly provides for exception to be made by regulation:

> Except as otherwise provided in regulations prescribed by the Secretary, the tax treatment of any subchapter S item shall be determined at the corporate level.

26 U.S.C. §6241. Likewise, the statute applying partnership tax procedures to subchapter S corporations expressly provides for modification and exception by

regulation:

> Certain partnership provisions made applicable.
>
> The provisions of
>
> (1) subchapter C which relate to ---
>
> (A) assessing deficiencies, and filing claims for credit or refund, with respect to partnership items, and
>
> (B) judicial determination of partnership items, and
>
> (2) so much of the other provisions of this subtitle as relate to partnership items are (except to the extend modified or made inapplicable in regulations) hereby extended to and made applicable to subchapter S items.

26 U.S.C. §6244 (emphasis added).

[4] Partnerships have an exception to entity level treatment for "small partnerships," of ten or fewer partners. 26 U.S.C. §6231(a)(1)(B). The Secretary promulgated a regulation creating a similar exception for small subchapter S corporations, with five or fewer shareholders. 26 C.F.R. §301.6241-1T(c). The regulation, however, does not apply to the tax year at issue:

> (c)(2) *Exception for small S corporations* - (I) *Effective date.* This paragraph (c)(2) shall apply to any taxable year of an S corporation the due date of the return for which

> (determined without regard to extensions) is on or after January 30, 1987.
>
> (ii) *Five or fewer shareholders.* For purposes of this paragraph (c), an S corporation shall not include a small S corporation with 5 or fewer shareholders, each of whom is a natural person or an estate ....

26 C.F.R. §301.6241-1T(c)(2). Thus, by its own terms, this regulation cannot benefit 2319 Creekside and Baldigo for the corporation's fiscal year ending June 30, 1984. The Secretary plainly considered earlier tax years, and decided not to apply the small subchapter S corporation to them, because subsection (a) of the same regulation provides for tax years beginning after December 31, 1982. 26 C.F.R. §301.6241-1T-(a).

[5] Baldigo argues, based on *Arenjay Corp. v. Commissioner*, 920 F.2d 269 (5th Cir. 1991), that notwithstanding the fact that the regulations do not help him, the small partnership exception of section 6231(a)(1)(B) applies through section 6244 to small S corporations. The Circuits have divided on this issue. The Fifth Circuit goes one way, in *Arenjay*, but the Tenth and Eleventh go the other, in *Home of Faith v. Commissioner*, 39 F.3d 263, 264 (10th Cir. 1994), and *Beard v. United States*, 992 F.2d 1516, 1523 (11th Cir. 1993). We join the Tenth and Eleventh Circuits.

[6] The Eleventh Circuit pointed out that section 6244 "does not incorporate every provision ... which relates to partnership

law. Rather it incorporates all provisions of the [law] which relate to *assessment of* partnership items, to *filing claims with respect to* partnership items, and to the *judicial determination of* partnership items," *Beard v. United States*, 992 F.2d 1516, 1523 (11th Cir. 1993)(emphasis in original). *Beard* distinguishes between "partnership items" and the definition of a partnership. *Id.* The term "partnership item" is a term of art, defined by statute at 26 U.S.C. §6231(a)(3). The term is defined so as not to include the definition of a partnership, where Congress put the exception for small partnerships. Thus §6244, which by its own terms applies only to "partnership items," does not apply to the small partnership exception to subchapter S corporations.

[7] Under §6241, Congress provided that tax determinations for S corporations would take place at the corporate level, except where the Secretary provided otherwise by regulations. Congress authorized the Secretary to change this by regulation, and the Secretary did so, but only for tax years subsequent to the one at issue. We therefore affirm the Tax Court's determination that there is no small S corporation exception to the entity level treatment for the 1984 tax year.

3. Other arguments

Mr. Baldigo argues that the IRS did not pay the United States Postal Service properly for its mailing services, so should be treated as though it had not properly mailed the notice in this case. But the notice was admittedly received and

responded to within the ninety day period, so the claimed defect in mailing is immaterial. *McKay v. Commissioner*, 886 F.2d 1237, 1238 (9th Cir. 1989).

Mr. Baldigo also argues that if he, not Mr. Rushton, was the tax matters person, then Mr. Rushton's stipulation as tax matters person to extend the statute of limitations was without effect. But Mr. Baldigo signed the stipulation too, albeit as "authorized representative" below Mr. Rushton's signature as "tax matters person," so the stipulation was effective whichever of them was the tax matters person. See Bugaboo Timber Co. v. Commissioner, 101 T.C. 31 (Nov. 22, 1993).

AFFIRMED.

Supreme Court, U.S.
FILED
DEC 28 1995
CLERK

No. 95-846

In the Supreme Court of the United States

OCTOBER TERM, 1995

ALVIS M. RUSHTON, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether a Subchapter S corporation with two shareholders is excepted from the unified audit and litigation procedures made applicable to S corporations by 26 U.S.C. 6241-6245.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A3) is unpublished, but the decision is noted at 60 F.3d 834 (Table). The opinion of the Tax Court (App., *infra*, 1a-4a) is unreported.[1]

JURISDICTION

The judgment of the court of appeals was entered on July 7, 1995. The petition for rehearing was denied on September 27, 1995 (Pet. App. A4-A5). The petition

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[1] The appendix to the petition does not include the opinion of the Tax Court, which is therefore included as an appendix to this brief.

for a writ of certiorari was filed on November 29, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner Alvis M. Rushton is the president of Twenty-Three Nineteen Creekside, Inc. (App., *infra*, 2a). Creekside has two shareholders (App., *infra*, 3a n.2) and validly elected to be taxed as an "S corporation" under Subchapter S of the Internal Revenue Code, 26 U.S.C. 1361-1379 (Pet. App. A9).

The Commissioner of Internal Revenue conducted an audit of Creekside's return for its fiscal year ending June 30, 1985. The audit was conducted pursuant to the unified S corporation audit and litigation procedures established under Sections 6221 through 6233 and Sections 6241 through 6245 of the Internal Revenue Code. 26 U.S.C. 6221-6233, 6241-6245. Upon completion of the audit, the Commissioner made adjustments to the return and issued a notice of final S corporation administrative adjustment (App., *infra*, 2a).

2. Petitioner sought review of the adjustments in Tax Court. Petitioner asserted (i) that, under 26 U.S.C. 6244, the corporation was excepted from the unified S corporation audit and litigation procedures because it had fewer than ten shareholders (App., *infra*, 1a, 3a) and (ii) that the notice of final S corporation administrative adjustment was therefore invalid.

The Tax Court rejected petitioner's assertions and entered a final decision based upon the parties' stipulation as to the appropriate adjustments to petitioner's June 30, 1985 return (App., *infra*, 1a). Under the terms of the stipulation, petitioner reserved the

right to appeal the ruling that the unified S corporation audit and litigation procedures applied.

3. The court of appeals affirmed (Pet. App. A1-A3), relying on its decision in the companion case of *Twenty-Three Nineteen Creekside, Inc.* v. *Commissioner*, 59 F.3d 130 (9th Cir. 1995). In that decision (Pet. App. A6-17), the court noted that Congress had provided an exception to the unified audit and litigation procedures for partnerships having fewer than ten partners (Pet. App. A14). See 26 U.S.C. 6231(a)(1)(B)(i). The court concluded, however, that Congress did not create an analogous exception from those procedures for Subchapter S corporations having fewer than ten shareholders (Pet. App. A16). In reaching that conclusion, the court followed (Pet. App. A15) the decision of the Tenth Circuit in *Home of Faith* v. *Commissioner*, 39 F.3d 263 (1994), cert. denied, 115 S. Ct. 2583 (1995), and the decision of the Eleventh Circuit in *Beard* v. *United States*, 992 F.2d 1516 (1993), and rejected the contrary decision of the Fifth Circuit in *Arenjay Corp.* v. *Commissioner*, 920 F.2d 269 (1991).

ARGUMENT

The decision of the Ninth Circuit in this case and those of the Tenth Circuit in *Home of Faith* v. *Commissioner* and the Eleventh Circuit in *Beard* v. *United States* conflict with the decision of the Fifth Circuit in *Arenjay Corp.* v. *Commissioner*. The question presented in this case, however, has insubstantial prospective importance. In 1987, acting pursuant to the substantive rulemaking authority provided by 26 U.S.C. 6241, the Secretary issued

Temp. Treas. Reg. § 301.6241-1T(c)(2)(ii).[2] That regulation established an exception to the unified audit and litigation procedures of the Code for Subchapter S corporations having five or fewer shareholders. That exception applies to all tax years for which the corporation's return is due on or after January 30, 1987. Temp. Treas. Reg. § 301.6241-1T(c)(2)(i).

1. a. In the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), Pub. L. No. 97-248, 96 Stat. 324, Congress established "unified" procedures that treat a partnership as an entity for purposes of audit and litigation concerning its reported income, deductions, and credits. 26 U.S.C. 6221-6233. Congress expressly excepted small partnerships from these unified audit and litigation procedures by defining the term "partnership" for this purpose to exclude partnerships having ten or fewer partners. 26 U.S.C. 6231(a)(1)(B)(i).

In the Subchapter S Revision Act of 1982 (SSRA), Pub. L. No. 97-354, § 4(a), 96 Stat. 1691, Congress further provided that the tax treatment of income, deductions, and credits of an S corporation is also generally to be determined at the corporation level in a unified proceeding, rather than in separate proceedings with respect to each shareholder. 26 U.S.C. 6241-6245.

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[2] Section 6244 (26 U.S.C.) provides that the unified audit provisions that "relate to partnership items, are (except to the extent modified or made inapplicable in regulations) hereby extended to and made applicable to subchapter S items." Section 6241 (26 U.S.C.) provides that "[e]xcept as otherwise provided in regulations prescribed by the Secretary, the tax treatment of any subchapter S item shall be determined at the corporate level."

Instead of enacting a specific set of audit and litigation procedures for S corporations, however, Congress extended and made applicable to "subchapter S items" the audit and litigation procedures applicable to "partnership items." 26 U.S.C. 6244. In particular, Section 6244 of the Code extends and makes applicable to Subchapter S items those provisions of Subchapter C (Sections 6221 through 6233 of the Code) that "relate to partnership items," including the provisions that relate to deficiencies with respect to partnership items, filing claims for credit or refund with respect to partnership items, and judicial determination of partnership items. 26 U.S.C. 6244.

b. The court of appeals correctly determined (Pet. App. A2, A15-A16) that Section 6244 of the Internal Revenue Code does not incorporate by reference the exception for small partnerships provided in Section 6231(a)(1)(B)(i). By its terms, Section 6244 extends and makes applicable to S corporation items only those provisions of Subchapter C that relate to "partnership items." 26 U.S.C. 6244. The exception for small partnerships in Section 6231(a)(1)(B)(i) is based upon the definition of a "partnership"; it does not involve the definition of "partnership items," a term that is separately defined in Section 6231(a)(3) of the Code. Compare 26 U.S.C. 6231(a)(1)(B)(i) with 26 U.S.C. 6231(a)(3). As the Eleventh Circuit explained in *Beard* v. *United States*, 992 F.2d at 1521:

> [S]ection 6244 does not incorporate section 6231(a)(1) into the SSRA. * * * [S]ection 6244 simply provides that an S corporation's income, loss, deductions, and credits are to be identified, computed, and contested pursuant to the same

> procedures that are used to identify, compute, and contest a partnership's items—namely, the unified audit and litigation procedures contained in [TEFRA]. Section 6244 does not purport to limit or define *who* must follow those procedures. It does not, by its terms, define S corporation. Rather, section 6244 merely prescribes *what* procedures must be followed when a dispute arises between the IRS and an S corporation's shareholders as to the S corporation's items, regardless of how S corporation is defined elsewhere in the Code.

Accord, *Home of Faith* v. *Commissioner*, 39 F.3d at 264.

In reaching the contrary conclusion in *Arenjay Corp.* v. *Commissioner*, 920 F.2d 269 (1991), the Fifth Circuit did not analyze these discrete statutory provisions. See *Beard* v. *United States*, 992 F.2d at 1522. Like the Tenth Circuit in *Home of Faith*, the court of appeals correctly followed the careful reasoning of the Eleventh Circuit in *Beard* and properly rejected *Arenjay*.

2. In Sections 6241 and 6244 of the Code, Congress authorized the Secretary to adopt regulations to establish exceptions to the unified audit and litigation provisions for Subchapter S corporations. See *Beard* v. *United States*, 992 F.2d at 1521; note 2, *supra*. In 1987, acting pursuant to that authority, the Secretary adopted Temp. Treas. Reg. § 301.6241-1T. See T.D. 8122, 1987-1 C.B. 342. Paragraph (c)(2) of the Regulation provides that, for taxable years for which returns are due on or after January 30, 1987, the term "S corporation shall not include a small S corporation," and then defines the term "small S corporation" to

mean an S corporation having five or fewer shareholders.

Following the adoption of this regulation, the question presented in this case would arise only with respect to Subchapter S corporations that have more than five and fewer than eleven shareholders. Even before the 1987 regulation was adopted, litigation concerning this issue was relatively sparse. For years after 1987, the question presented in this case has only a remote significance (and would arise in a legal context altered by the regulation). Further review does not appear warranted at this time.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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DECEMBER 1995

APPENDIX

T.C. MEMO 1993-179

UNITED STATES TAX COURT

DOCKET NO. 4787-90

TWENTY-THREE NINETEEN CREEKSIDE, INC., ALVIS MINICK RUSHTON, TAX MATTERS PERSON, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

[Filed April 22, 1993]

MEMORANDUM OPINION

FAY, *Judge*: A number of issues have been settled by the parties, and the only issue now in dispute is whether Twenty-Three Nineteen Creekside, Inc. (hereinafter 2319 Creekside), is subject to the unified audit and litigation procedures under the provisions of subchapter D, chapter 63, subtitle F, of the Internal Revenue Code of 1954 (tax treatment of Subchapter S items). Once this Court resolves this underlying issue, the parties have stipulated the results which follow therefrom. We therefore restrict ourselves to answering the question posed by the parties.

All section references are to the Internal Revenue Code in effect for the year in issue, and all Rule references are to the Tax Court Rules of Practice and Procedure, unless otherwise indicated. The parties have submitted this case fully stipulated and the facts so stipulated are found accordingly. By this reference, the stipulation of facts and attached exhibits are incorporated into this opinion. This Court allowed the parties to file their previously submitted trial memoranda as briefs of their respective positions.

For fiscal year ended June 30, 1985, 2319 Creekside's principal place of business was in Santa Rosa, California. During the year at issue 2319 Creekside had no more than two shareholders.

On August 20, 1985, Alvis M. Rushton, as president of 2319 Creekside, timely filed a Federal income tax return (Form 1120S) for the fiscal year ended June 30, 1985. Respondent examined that return under the unified audit and litigation procedures. A notice of final S corporation administrative adjustment (FSAA) was mailed to Alvis M. Rushton, tax matters person of 2319 Creekside, on December 31, 1989. The schedules attached to the FSAA indicate a disallowance of deductions for the year in the amount of $183,792.

In *Eastern States Casualty Agency, Inc. v. Commissioner*, 96 T.C. 773, 782 (1991), we held that there is no small S corporation exception to the unified audit and litigation procedures prior to January 30, 1987, the effective date of section 301.6241-1T(c), Temporary Proced. & Admin. Regs., 52 Fed. Reg.

3003 (Jan. 30, 1987).[1] This Court has continued to follow this view in subsequent cases. *Twenty-Three Nineteen Creekside, Inc. v. Commissioner*, T.C. Memo. 1991-271 (fiscal year ended June 30, 1984, of 2319 Creekside); *Cichy v. Commissioner*, T.C. Memo. 1991-270.

Petitioner contends that we should not follow the rationale set out above but should either : (1) Follow *Arenjay Corp. v. Commissioner*, 920 F.2d 269 (5th Cir. 1991), revg. and remanding an unreported Order of this Court; or (2) craft an exception for one-shareholder S corporations to the unified audit and litigation provisions.[2] However, both of these conten-

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[1] The Temporary Regulations provide that, where an S corporation consists of five or fewer shareholders, the tax treatment shall not be determined at the corporate level. The Temporary Regulations, however, are applicable only to the taxable year of an S corporation, the due date of the return of which is on or after Jan. 30, 1987. Sec. 301.6241-1T(c)(2)(i), Temporary Proced. & Admin. Regs., 52 Fed. Reg. 3003 (Jan. 30, 1987). However, the year before us is fiscal year ended June 30, 1985. By its terms, the Temporary Regulations are inapplicable to the issue at hand.

[2] During fiscal year ended June 30, 1985, petitioner contends that the corporation had no more than one shareholder for any period during the year. (Michael E. Baldigo was the 100-percent owner during the first 3 months of the fiscal year, and Alvis M. Rushton was the 100-percent owner during the last 9 months.) The burden of proof is on petitioner. Rule 142(a); *Welsh v. Helvering*, 290 U.S. 111, 115 (1933). Petitioner has presented no evidence on this issue. The Form 1120S and Schedules K-1 indicate Twenty-Three Nineteen Creekside, Inc. (hereinafter 2319 Creekside), had two shareholders during the year at issue. Additionally, the parties stipulated "Michael E. Baldigo owned a 25% interest and Alvis M. Rushton owned

tions were addressed in *Eastern States Casualty Agency, Inc. v. Commissioner*, *supra* at 782, wherein we respectfully declined to follow the Court of Appeals for the Fifth Circuit's decision in *Arenjay Corp. v. Commissioner*, *supra*, and stated we would not longer follow this Court's opinion in *Blanco Investments & Land, Ltd. v. Commissioner*, 89 T.C. 1169 (1987) (which supported petitioner's one-shareholder S corporation exception). As we have previously stated, "There are no exceptions written into the statutory language for subchapter S corporations based upon the number of shareholders." *Eastern States Casualty Agency, Inc. v. Commissioner*, *supra* at 782. "Congress has chosen to leave the question of exceptions to the discretion of the Secretary." *Id.*

Thus, for the year ended June 30, 1985, we find respondent correctly utilized the unified audit and litigation provision when issuing the FSAA to Alvis M. Rushton as Tax Matters Person for 2319 Creekside.

To reflect the foregoing,

Decision will be entered for respondent.

75% interest." Although it would not change our current opinion, we find 2319 Creekside had two shareholders.